

Message Text

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ACTION EB-08

INFO OCT-01 EA-07 ISO-00 AID-05 CIAE-00 COME-00 FRB-03

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R 290700Z MAR 77

FM AMEMBASSY MANILA

TO SECSTATE WASHDC 7697

AMCONSUL HONG KONG

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HONG KONG FOR REGIONAL TREASURY REPRESENTATIVE

E. O. 11652: NA

TAGS: EFIN, EINV, RP

SUBJECT: GOP CONTEMPLATES LIMITATION OF FOREIGN COMPANY CREDIT

1. SUMMARY. A DRAFT CENTRAL BANK CIRCULAR WOULD LIMIT ACCESS TO CREDIT BY FOREIGN COMPANIES BY ESTABLISHING A FIXED DEBT/EQUITY RATIO WHICH SUCH COMPANIES MUST MEET. THE INTENTION IS TO INCREASE ACCESS TO DOMESTIC CREDIT BY PHILIPPINE BORROWERS, BUT SUCH A RESULT IS BY NO MEANS ASSURED. A MEETING CALLED TO DISCUSS THE DRAFT REVEALED DISSATISFACTION WITH THE DRAFT AND A FEELING THAT IT WILL NOT ACCOMPLISH ITS INTENDED RESULT. FOREIGN COMPANIES GENERALLY ARE NOT HAPPY WITH THE PROSPECT OF A NEW CONDITION OF DOING BUSINESS IN THE PHILIPPINES. SOME FORM OF FOREIGN COMPANY CREDIT LIMITATION HAS BEEN UNDER CONSIDERATION FOR ABOUT TWO YEARS, HOWEVER, AND THE GOP APPEARS DETERMINED TO MOVE FORWARD. REGUALTIONS MAY BE IN PLACE BY MID-YEAR. END SUMMARY.

2. THE ISSUE OF ACCESS TO CREDIT BY FOREIGN FIRMS IN

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THE PHILIPPINES IS CONTENTIOUS AND HAS BEEN UNDER STUDY FOR SOME TWO YEARS. PROPONENTS OF SOME SCHEME OF LIMITING THE DOMESTIC CREDIT AVAILABLE TO FOREIGN COMPANIES HAVE BASED THEIR APPROACH ON THE NOTION THAT THESE COMPANIES CONSTITUTE UNFAIR COMPETITION FOR SCARCE CREDIT RESOURCES, THUS RAISING THE COST OF CREDIT TO SMALLER INDIGENOUS FIRMS OR FORCING THEM OUT ENTIRELY.

OPPONENTS OF CREDIT LIMITATION HAVE MAINTAINED THAT THE SMALLER FIRMS, BEING GREATER CREDIT RISKS, WILL ALWAYS PAY MORE FOR THE USE OF MONEY, REGARDLESS OF HOW CREDIT IS RATIONED.

3. THE ISSUE RATHER UNEXPECTEDLY RESURFACED RECENTLY WITH THE CIRCULATION OF DRAFT REGULATIONS PRODUCED BY THE GOP'S JOINT COMMITTEE ON FOREIGN COMPANY CREDITS, CHAIRED BY THE BOARD OF INVESTMENTS (BOI). THE DRAFT WAS DISCUSSED AT A GENERAL MEETING ON MARCH 25, TO WHICH WERE INVITED REPRESENTATIVES OF FOREIGN MISSIONS, BANKS, COMMERCE AND TRADE ORGANIZATIONS, AND CORPORATIONS.

4. BRIEFLY, THE PROPOSED CENTRAL BANK CIRCULAR APPROACHES THE CREDIT ISSUE FROM THE DIRECTION OF FIXED DEBT/EQUITY RATIOS. FOREIGN FIRMS (I.E., MORE THAN 40 0/0 FOREIGN-OWNED) IN PREFERRED AREAS OF ACTIVITY SPECIFIED IN THE REGULATION MUST MAINTAIN A 60/40 DEBT/EQUITY RATIO; THOSE IN OTHER AREAS OF MANUFACTURING, 55/45; AND ALL OTHERS, 50/50. AS LONG AS A FIRM HAS DOMESTIC BORROWINGS OUTSTANDING, APPLICATION FOR OUTWARD REMITTANCE OF PROFITS, EARNINGS, OR DIVIDENDS WILL NOT BE APPROVED UNLESS THE PRESCRIBED DEBT/EQUITY RATIO IS MET. EXISTING FOREIGN FIRMS WILL HAVE THREE YEARS IN WHICH TO BEEF UP THEIR EQUITY TO MEET THE PRESCRIBED RATIOS. BANKS AND OTHER FINANCIAL INTERMEDIARIES ARE EXEMPT FORM THE CIRCULAR.

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5. AT THE MARCH 25 DISCUSSION SESSION, BOI GOVERNOR TORDESILLAS, WHO IS CHAIRMAN OF THE COMMITTEE, SAID THAT PREVIOUS CREDIT LIMITATION PROPOSALS WERE DISCARDED AS TOO COMPLEX, AND THAT THIS "POSITIVE" DEBT/EQUITY APPROACH IS SIMPLE AND WORKABLE. HE ALSO TOOK THE HIGH GROUND BY INSISTING THAT NO ONE COULD QUESTION THE PRINCIPLE THAT FOREIGN FIRMS SHOULD BRING IN ADEQUATE CAPITAL. NO ONE IN FACT CHALLENGED THAT PRINCIPLE. FORMER AMCHAM PRESIDENT GEORGE SUTER ASSERTED THAT THE NEW DRAFT REPRESENTED A NEW THRUST AND THAT THERE HAD BEEN INSUFFICIENT TIME FOR STUDY. (THE DRAFT WAS DISTRIBUTED ONLY ON MARCH 23). TORDESILLAS COUNTERED THAT THE OBJECTIVE REMAINED THE SAME AS BEFORE--TO INSURE AVAILABILITY OF LOCAL CREDIT TO PHILIPPINE FIRMS. CITIBANK MANAGER DAN JACOBSEN AND

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OTHERS SUGGESTED THAT THE REGULATION MIGHT HAVE THE OPPOSITE EFFECT TO THAT INTENDED--THAT FIRMS WHICH ARE ACCUSTOMED TO BORROW IN ORDER TO EXTEND CREDIT TO SUPPLIERS OR DEALERS WILL NOW HAVE TO RESTRICT THAT CREDIT. COMMITTEE REACTION TO THIS WAS UNSYMPATHETIC, AND IT WAS SUGGESTED THAT THE FIRM SHOULD SIMPLY INCREASE EQUITY AS INTENDED BY THE TERMS OF THE REGULATION OR POSSIBLY TRANSFER THE CREDIT FUNCTION TO OTHER INSTITUTIONS. OTHER QUESTIONING DEALT WITH TECHNICAL ASPECTS OF APPLYING THE PROPOSED CIRCULAR. NO ONE QUESTIONED THE SPECIFIC DEBT/EQUITY RATIOS THEMSELVES, WHICH TORDESILLAS CLEARLY INDICATED ARE NEGOTIABLE.

6. PRIVATE COMMENT ON THE DRAFT CIRCULAR HAS RANGED FROM INDIFFERENCE TO DIRE EXPECTATIONS OF A BREAKDOWN IN THE CREDIT SYSTEM, THOUGH WITH NO CLEAR VISION OF WHY SUCH UNFORTUNATE CONSEQUENCES SHOULD RESULT. SOME FIRMS WILL CLEARLY BE MORE AFFECTED THAN OTHERS, PARTICULARLY THOSE WHICH EXTEND BUYER OR SUPPLIER CREDIT (E.G., OIL AND TIRE COMPANIES), AND THE COMMITTEE CLEARLY RECOGNIZED LIMITED OFFICIAL USE

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THAT SOME FOREIGN FIRMS MAY SUFFER A COMPETITIVE DISADVANTAGE VIS-A-VIS DOMESTIC COMPANIES AS A RESULT OF THESE REGULATIONS. SOME BANKERS PREDICT UNFAVORABLE ECONOMIC

EFFECTS--AN OVERALL CONSTRICTION OF CREDIT WITH NO MORE FUNDS THAN NOW AVAILABLE TO SMALL LOCAL FIRMS AND AT NO CHEAPER RATES. MUCH SPECULATION CENTERS ON THE MANNER IN WHICH REGULATIONS WILL BE APPLIED, WITH A CONSENSUS THAT APPLICATION IS LIKELY TO BE RELAXED.

7. TORDESILLAS SOLICITED WRITTEN COMMENTS WITHIN TEN DAYS, AND STATED THAT THE COMMITTEE MUST SUBMIT A FINAL DRAFT TO THE MONETARY BOARD IN 30 DAYS. HE EXPECTS A REGULATION TO BE IN EFFECT SOME TIME AFTER JUNE.

8. COMMENT: NO ONE SEEMS VERY SURE WHAT THE EFFECTS OF THE PROPOSED CIRCULAR WOULD BE ON THE OVERALL CREDIT PICTURE. SIMILARLY, NO CLEAR CONSENSUS HAS EMERGED AMONG FOREIGN COMPANIES, PERHAPS BECAUSE OF THE SHORT TIME AVAILABLE FOR STUDYING THE DRAFT CIRCULAR. SOME FACE THE PROSPECT OF BRINGING IN MAJOR INFUSIONS OF NEW EQUITY CAPITAL OR OF FINDING NEW WAYS OF DOING BUSINESS. AT THE LEAST, THIS MOVE WILL CONSTITUTE A NEW IRRITANT TO FOREIGN COMPANIES IN THE PHILIPPINES. BUT THE GOP SEEMS BENT ON ENACTING SOME FORM OF REGULATION, AND AS TORDESILLAS STATED, IF FOREIGN COMPANIES DO NOT WISH TO BRING IN ADEQUATE CAPITAL, THAT IS "PROBABLY NOT THE KIND OF FOREIGN COMPANY THAT THE PHILIPPINES WANTS ANYWAY."
SULLIVAN

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